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No. 328

In the Supreme Court of the United States

OCTOBER TERM, 1941

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

ALABAMA ASPHALTIC LIMESTONE COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

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The Acting Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Fifth Circuit, entered in the above case on May 5, 1941, affirming a decision of the United States Board of Tax Appeals.

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 33–54) is published at 41 B. T. A. 324. The opinion of the Circuit Court of Appeals (R. 154–157) is reported in 119 F. (2d) 819.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered May 5, 1941 (R. 157). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Pursuant to plan, corporate assets were bought in by a creditors' committee at bankruptcy sale. The property was transferred to the taxpayer, a new corporation, which issued its preferred and common stock to participating creditors. The question is whether the basis of the assets for purposes of computing depreciation and depletion is the same as it would be in the hands of the old corporation under Section 113 (a) (7) of the Revenue Act of 1934. The answer depends upon whether the transaction constituted a "reorganization" within the definition of Section 112 (i) (1) of the Revenue Act of 1928.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra*, pp. 7–8.

STATEMENT

Alabama Rock Asphalt, Inc., the taxpayer's predecessor corporation (hereafter referred to as Alabama) was a wholly owned subsidiary of the Deep Water Coal & Iron Corporation. In 1929–

1930 it had outstanding various unsecured notes, issued in return for advances made by individual stockholders of the parent corporation. These notes were to mature February 1, 1930, with the exception of one which was to mature April 14, 1929[1] (R. 34–35).

Following a failure to obtain the agreement of all noteholders to take stock in the company at the maturity of their claims, a creditors' committee was formed late in 1929, and a plan was proposed to which all except two of the creditors assented. The plan provided for the formation of a new corporation, which would acquire Alabama's assets. The stock of the new corporation, consisting of preferred and common stock, would be issued to the old creditors (R. 35–36).

With the assent of the creditors, except for the two dissenters, involuntary proceedings in bankruptcy were instituted on September 11, 1930, and a trustee appointed. The appraised value of the bankrupt's assets was $155,876.52 (R. 36); as of December 31, 1930, its liabilities, consisting of the notes and sundry other obligations, aggregated $838,690.51 (R. 37).

The trustee in bankruptcy offered the assets for sale at public auction on January 8, 1931, and they were bought in by the committee for $150,000 (R. 37). It appears from the trustee's report that the

[1] The latter note was endorsed by the parent corporation and secured by all the stock of Alabama (R. 35).

committee deposited $15,000 in cash, offered to deliver in part payment the agreement of the creditors to take stock of the new company in satisfaction of their claims, and also offered to pay in cash any balance necessary to meet costs of administration, etc., and a dividend to nonassenting creditors (R. 37).

Thereafter, the taxpayer was formed and acquired the bankrupt's assets. In accordance with the plan, its stock was issued to the assenting creditors, representing approximately 92% of the total claims (R. 37–38).

In computing its depreciation and depletion allowances for the year 1936, the taxpayer treated its assets as having the same basis that they had in the hands of the old corporation. The Commissioner, in determining the deficiency, used the cost of the assets to the committee as their basis, namely the price paid at the bankruptcy sale. The Board of Tax Appeals rejected the Commissioner's position, and the court below affirmed.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

(1) In holding that the taxpayer's assets had been acquired in connection with a "reorganization" of Alabama and that, therefore, the basis was the same as it would be in the hands of that company.

(2) In failing to hold that the basis of the assets was the cost to the creditors' committee at the bankruptcy sale.

(3) In sustaining the decision of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

The basic question presented in the case is the same as that involved in *Commissioner* v. *Bondholders Committee, Marlborough Investment Co.*, 118 F. (2d) 511 (C. C. A. 9th), pending on the taxpayers' petition for certiorari, Nos. 128, 129, and *Commissioner* v. *Southwest Consol. Corp.*, 119 F. (2d) 561 (C. C. A. 5th), pending on the Government's petition for certiorari, No. 286. The general importance of the problem in the administration of the revenue laws and the conflict between the Fifth and the Ninth Circuits have been pointed out in the Government's petition in the *Southwest* case.

The considerations for further review have since been accentuated by the decisions of the Circuit Courts of Appeals for the Second and Eighth Circuits in *Commissioner* v. *New Haven & Shore Line Ry Co.*, 1941 Prentice-Hall, par. 62841, and *Commissioner* v. *New President Corp.*, 1941 Prentice-Hall, par. 62831, respectively. In the *New Haven* case (decided July 16, 1941), the court, like the court below, sustained the holding of the Board of Tax Appeals that there was a "reorganization" within the meaning of the revenue laws. In the

New President case (decided July 14, 1941), the court agreed with the Commissioner that there was not a "reorganization", but affirmed the result reached by the Board by adopting as the basis for computing depreciation and gain or loss upon resale of the property its market value at the time of acquisition rather than the price paid for the property at the foreclosure sale.[2]

CONCLUSION

The petition should be granted.

Respectfully submitted.

CHARLES FAHY,
Acting Solicitor General.

JULY 1941.

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[2] This result was reached by the application of Regulations 77, Art. 193, and Regulations 94, Art. 23 (k)–3, which provide:

"In addition, where ["if" in place of "where" in Regulations 94] the creditor buys in the mortgaged or pledged property, loss or gain is realized measured by the difference between the amount of those obligations of the debtor which are applied to the purchase or bid price of the property (to the extent that such obligations constitute capital or represent an item the income from which has been returned by him) and the fair market value of the property. The fair market value of the property shall be presumed to be the amount for which it is bid in by the taxpayer in the absence of clear and convincing proof to the contrary. If the creditor subsequently sells the property so acquired, the basis for determining gain or loss is the fair market value of the property at the date of acquisition. * * *"

APPENDIX

Revenue Act of 1928, 45 Stat. 791:

SEC. 112. RECOGNITION OF GAIN OR LOSS.

* * * * *

(i) *Definition of reorganization.*—As used in this section and sections 113 and 115—

(1) The term "reorganization" means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantiallly all the properties of another corporation), * * *

Revenue Act of 1934, 48 Stat. 680:

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (Unadjusted) of Property.*—The basis of property shall be the cost of such property; except that—

* * * * *

(7) *Transfers to corporation where control of property remains in same persons.*—If the property was acquired after December 31, 1917, by a corporation in connection with a reorganization, and immediately after the transfer an interest or control in such property of 50 per centum or more remained in the same persons or any of them, then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor

upon such transfer under the law applicable to the year in which the transfer was made. This paragraph shall not apply if the property acquired consists of stock or securities in a corporation a party to the reorganization, unless acquired by the issuance of stock or securities of the transferee as the consideration in whole or in part for the transfer.

* * * * * *

(b) *Adjusted Basis.*—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

* * * * * *

(U. S. C., Title 26, Sec. 113.)

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

(a) *Basis for Depreciation.*—The basis upon which exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be the adjusted basis provided in section 113 (b) for the purpose of determining the gain upon the sale or other disposition of such property.

(b) *Basis for Depletion.*—

(1) *General rule.*—The basis upon which depletion is to be allowed in respect of any property shall be the adjusted basis provided in section 113 (b) for the purpose of determining the gain upon the sale or other disposition of such property, except as provided in paragraphs (2), (3), and (4) of this subsection.

* * * * * *

(U. S. C., Title 26, Sec. 114.)

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